CALIFORNIA INFRASTRUCTURE AND ECONOMIC DEVELOPMENT BANK (I-Bank)
EXEMPT FACILITY REVENUE BOND FINANCING PROGRAM

STAFF REPORT

<table>
<tr><th colspan="4">EXECUTIVE SUMMARY</th></tr>
<tr><td>Applicant:</td><td>Pacific Gas and Electric Company (PG&E)</td><td>Amount Requested:</td><td>Not to exceed $308,550,000</td></tr>
<tr><td rowspan="3">Applicant Description:</td><td rowspan="3">PG&E, one of the largest investor-owned natural gas and electric utilities in the United States, serving approximately 5.1 million electricity distribution customers and approximately 4.3 million natural gas distribution customers throughout northern and central California.</td><td>Date of Board Meeting:</td><td>July 28, 2009</td></tr>
<tr><td>Type of Issue:</td><td>Refunding</td></tr>
<tr><td>Resolution Number:</td><td>09-26</td></tr>
<tr><td>Project Site:</td><td>Geysers Geothermal Power Plant with locations within Sonoma, Mendocino and Lake Counties, and Diablo Canyon Nuclear Power Plant located on the Pacific Coast Highway near San Luis Obispo.</td><td colspan="2">Prepared by: Paula Connors, Andrea Kennedy and Joel Tokimitsu</td></tr>
<tr><td>Project Description:</td><td colspan="3">I-Bank bonds (2009 Bonds) to be issued to refund bonds previously issued by the I-Bank in 2008 (2008 Bonds) to take advantage of a provision of the federal American Recovery and Reinvestment Act (ARRA) permitting the refunding of tax-exempt bonds bearing interest that is subject to the Alternative Minimum Tax (AMT) through the issuance of bonds bearing interest that is not subject to the -AMT.</td></tr>
<tr><td>Uses of Bond Proceeds:</td><td colspan="3">Bond proceeds will be used to refund the 2008 Bonds.</td></tr>
<tr><td>Public Benefits:</td><td colspan="3">PG&E estimates that the more favorable tax treatment of the interest on the proposed 2009 Bonds will result in a savings of approximately 0.10% to 1.00% in annual debt service costs over the next seventeen years. PG&E reports that it estimates this savings in debt service costs corresponds to estimated ratepayer savings ranging from $5,000,000 to $50,000,000 in the same period.</td></tr>
</table>

Financing Structure:

Type of Issue:	Publicly-offered variable rate demand bonds issued in one or more series, in minimum denominations of $100,000 or any integral multiple of $5,000 in excess thereof.
Tax Status:	Tax-exempt, non-AMT, exempt facility bonds.
Term:	7 to 17 years.
Credit Enhancement:	Letter of credit from Wells Fargo Bank, N.A.
Credit Rating:	Expected AAA/A-1+ by Standard and Poor's and Aa1/VMIG1 by Moody's Investors Service based upon the credit rating of Wells Fargo Bank, N.A.

Total Est. Sources of Funds:		**Total Est. Uses of Funds*:**	
2009 Bond	$308,550,000	2008 Bonds	$308,550,000
TOTAL SOURCES	**$308,550,000**	**TOTAL USES**	**$308,550,000**

Financing Team:

Bond Counsel:	Sidley Austin, LLP
Borrower Counsel:	Orrick Herrington & Sutcliffe
Underwriters:	Morgan Stanley & Co. Inc., Merrill Lynch Pierce Fenner & Smith Inc., and Wachovia Bank National Association
Trustee:	Deutsche Bank Trust Company
Special Counsel to I-Bank:	Stradling Yocca Carlson & Rauth

Staff Recommendation:
Staff recommends approval of Resolution 09-26 authorizing the issuance of refunding bonds in an amount not to exceed $308,550,000 for the benefit of Pacific Gas and Electric Company.

PROJECT DESCRIPTION / FINANCING STRUCTURE

The purpose of this financing is to refund $308,550,000 of California Infrastructure and Economic Development Bank Refunding Revenue Bonds (Pacific Gas and Electric Company) Series 2008A – Series 2008D (2008 Bonds).

The 2008 Bonds bear interest that is subject to Alternative Minimum Tax (AMT). The AMT classifies tax-exempt interest on certain private activity bonds as a preference item to be included in the calculation of the bondholder's Federal income tax obligation. The American Recovery and Reinvestment Act (ARRA) authorizes issuers to issue bonds that bear interest that is not subject to the AMT (referred to as "non-AMT bonds") for the purpose of refunding "AMT bonds". As a result of these provisions of the ARRA, PG&E now has the opportunity to convert the 2008 Bonds to non-AMT bonds.

PG&E proposes to refund the 2008 Bonds by issuing non-AMT variable rate demand obligations (2009 Bonds), secured by PG&E's obligation to pay loan payments in the amount due on the 2009 BOnds, and by a direct pay letter of credit from Wells Fargo Bank, N.A. The 2009 Bonds will be publicly offered to investors and are expected to carry a rating of AAA/A-1+ by Standard and Poor's and Aa1/VMIG1 by Moody's Investor Service based upon the credit rating of Wells Fargo Bank, N.A. The 2008 Bonds refunded bonds issued by the I-Bank in 2005, which were issued to refund bonds issued by the California Pollution Control Financing Authority in prior years (see Exhibit A – I-Bank Staff Report for the August 21, 2008 Board meeting for information about the prior bond issuances).

Each series of the 2009 Bonds shall constitute a special obligation of the I-Bank, payable solely from revenues provided under a loan agreement between the I-Bank and PG&E. Neither the faith and credit nor the taxing power of the I-Bank, the State or any political corporation, subdivision or agency of the State will be pledged to the payment of the principal of, premium, if any, or interest on the 2009 Bonds, nor shall the the State or any political corporation, subdivision or agency of the State (except the I-Bank to the extent of its limited obligation) be liable or obligated to pay the principal of, premium, if any, or interest on, the 2009 Bonds.

PUBLIC BENEFITS

Pursuant to a long-standing commitment by PG&E, ensured by the regulatory oversight of the CPUC, PG&E's electric and gas rates are set to cover PG&E's interest expenses. The vehicle for passing the benefit of the cost savings of this proposed refunding along to PG&E customers is the CPUC's annual cost of capital proceeding. In that proceeding, PG&E provides a listing of all its outstanding debt, as well as any projected changes, for the CPUC's review and approval. The interest expense that is approved by the CPUC is then incorporated into electric and gas rates charged to customers. To date, PG&E estimates that the CPCFA Bonds, prior I-Bank Bonds have saved PG&E California customers as much as $7.9 million per year in interest expense, compared to taxable or corporate debt.

Furthermore, PG&E estimates the refunding of the 2008 Bonds with the non-AMT 2009 Bonds will result in a savings of approximately 0.10% to 1.00% in annual debt service costs over the next seventeen years. PG&E estimates that this savings in debt service costs corresponds to estimated ratepayer savings ranging from $5,000,000 to $50,000,000 in the same period.

OTHER PROJECT DATA

PERMITS AND APPROVAL	
Required?	☒ **NO** ☐ **YES, Describe:**
TEFRA	
Date of TEFRA hearing	TEFRA hearings are not required for refunding bonds.
Publications	N/A
Oral/Written Comments	☐ **NO** ☐ **YES, Explain:**
LEGAL QUESTIONNAIRE	
Completed?	☐ **NO** ☒ **YES**
Issues?	☒ **NO** ☐ **YES, Explain:** PG&E has numerous lawsuits outstanding at any given time. As a publicly traded and regulated corporation, material information concerning the financial position and pending lawsuits and investigations are available to the public.
ELIGIBILITY REVIEW	
Project meets Public Interest Criteria (per G.C. §63046) ☒ **YES** ☐ **NO**	1. The Project is in the State of California. 2. PG&E is capable of meeting its obligations incurred under the proposed loan agreements, and, in particular as to its loan repayment obligations which secure the 2009 Bonds, based upon its ability to satisfy the requirements imposed by Wells Fargo Bank which is issuing a letter of credit which will support a rating on the Bonds at the time of issuance of at least "A3" from Moody's Investors Service, or "A-" from Standard & Poor's or Fitch, Inc., respectively, and (ii) the fact that the Borrower's senior notes, which are not supported by any credit enhancement, are assigned a rating of "A3" by Moody's Investors Service. Payments to be made by PG&E to the I-Bank under the proposed loan agreement are adequate to pay the current expenses of the I-Bank in connection with the financing and to make all the scheduled payments on the 2009 Bonds. 2. The proposed financing is appropriate for the Project. 3. The Project is consistent with any existing local or regional comprehensive plans.
The Project meets the Policies and Procedures for Conduit Revenue Bond Financing for Economic Development Facilities established as guidelines for I-Bank Staff by the Board: ☒ **YES** ☐ **NO**	
INDUCEMENT CERTIFICATE	
Completed?	☐ **NO** ☐ **YES** Certificate No.: ☒ **N/A** Date:

RECOMMENDATION

Staff recommends approval of Resolution 09-26, authorizing the issuance of bonds in an amount not to exceed $308,550,000 for the benefit of Pacific Gas and Electric Company.

EXHIBIT A

EXHIBIT A

August 21, 2008 PG&E Staff Report

CALIFORNIA INFRASTRUCTURE AND ECONOMIC DEVELOPMENT BANK (I-Bank) EXEMPT FACILITY REVENUE BOND FINANCING PROGRAM

STAFF REPORT

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<tr><th colspan="4">EXECUTIVE SUMMARY</th></tr>
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<tr><td rowspan="3">Applicant Description:</td><td rowspan="3">PG&E, one of the largest investor-owned natural gas and electric utilities in the United States, serving approximately 5.1 million electricity distribution customers and approximately 4.3 million natural gas distribution customers throughout northern and central California.</td><td>Date of Board Meeting:</td><td>August 21, 2008</td></tr>
<tr><td>Type of Issue:</td><td>Exchange/Refunding</td></tr>
<tr><td>Resolution Number:</td><td>08-25</td></tr>
<tr><td>Project Site:</td><td>Geysers Geothermal Power Plant with locations within Sonoma, Mendocino and Lake Counties, and Diablo Canyon Nuclear Power Plant located on the Pacific Coast Highway near San Luis Obispo.</td><td colspan="2">Prepared by: Tara Dunn and Andrea Kennedy</td></tr>
<tr><td>Project Description:</td><td colspan="3">The I-Bank previously issued auction rate securities in 2005 (2005 Bonds) to repay loans used to pay-off prior bonds issued by the California Pollution Control Financing Authority as a result of PG&E's bankruptcy filing in 2001. The 2005 Bonds have all been repurchased by PG&E in accordance with US Treasury guidelines.</td></tr>
<tr><td>Uses of Bond Proceeds:</td><td colspan="3">Bond proceeds (2008 Bonds) will be used to replace the 2005 Bonds through an exchange. Once the 2008 Bonds are exchanged for the 2005 Bonds, the 2005 Bonds will be cancelled.</td></tr>
<tr><td>Public Benefits:</td><td colspan="3">PG&E estimates that the proposed tax-exempt refunding bonds will enable it to save ratepayers approximately $55 million in interest, on a present value basis, over the next 18 years.</td></tr>
</table>

Financing Structure:

Type of Issue: Once exchanged, it is expected that the 2008 Bonds will be resold on the secondary market as a combination of publicly-offered variable-rate demand bonds and fixed rate demand bonds.

Tax Status: Tax-exempt, exempt facility bonds.

Term: 8 to 18 years.

Credit Enhancement: Unenhanced and/or secured with direct-pay letters of credit.

Credit Rating: The 2008 Bonds will be issued directly to PG&E. The underlying credit ratings of PG&E are currently A3/BBB+/A by Moody's, Standard & Poor's and Fitch, respectively.

Total Est. Sources of Funds:		**Total Est. Uses of Funds*:**	
2008 Bond Proceeds	$453,550,000	2005 Bonds	$453,550,000
TOTAL SOURCES	**$453,550,000**	**TOTAL USES**	**$453,550,000**

**Costs of issuance will be paid by PG&E from other sources of funds.*

Financing Team:

Bond Counsel: Sidley Austin, LLP

Borrower Counsel: Orrick Herrington & Sutcliffe

Underwriter's Counsel: Ballard Spahr Andrew & Ingersoll

Trustee: Deutsche Bank Trust Company

EXHIBIT A

Staff Recommendation:
Staff recommends approval of Resolution 08-25 for an amount not to exceed $453,550,000 for Pacific Gas and Electric Company.

BACKGROUND AND HISTORY

Incorporated in 1905, Pacific Gas and Electric Company (PG&E) is a public utility operating in northern and central California. PG&E engages in the businesses of electricity and natural gas distribution, electricity generation, procurement and transmission, and natural gas procurement, transportation and storage. On January 1, 1997, PG&E Corporation became the holding company of PG&E and its subsidiaries.

Electricity and Natural Gas Distribution. As of December 31, 2007, PG&E served approximately 5.1 million electricity distribution customers and approximately 4.3 million natural gas distribution customers. In 2007, PG&E delivered approximately 86,179 gigawatt hours (GWh) of electricity, which included approximately 6,723 GWh transmitted to direct access customers, and delivered approximately 875 billion cubic feet (Bcf) of natural gas, which included approximately 605 Bcf of natural gas that PG&E did not purchase but transports on behalf of its customers.

Electricity Generation. PG&E owns, operates and controls an extensive hydroelectric system in northern and central California and the Diablo Canyon nuclear power plant located near San Luis Obispo, California. As of December 31, 2007, PG&E's electricity generation portfolio consisted of approximately 6,271 megawatts of owned generating capacity.

Electricity Transmission. PG&E owns and operates an electricity transmission system that comprises most of the high-voltage electricity transmission lines and facilities in northern and central California. PG&E's high-voltage transmission system currently consists of approximately 18,680 circuit miles of interconnected electricity transmission lines and support facilities.

Natural Gas Procurement Transportation and Storage. PG&E also owns and operates a natural gas pipeline and storage system that extends throughout all or part of 39 of California's 58 counties and includes most of northern and central California. This system currently consists of approximately 41,805 miles of distribution pipelines, 6,393 miles of backbone and local transmission pipelines and three storage facilities.

PG&E is regulated primarily by the California Public Utilities Commission (CPUC) and the Federal Energy Regulatory Commission (FERC). Among other things, the CPUC has jurisdiction to set the rates, terms and conditions of service for PG&E's electricity distribution, natural gas distribution and natural gas transportation and storage services in California. Ratemaking for retail sales from PG&E's generation facilities is also under the jurisdiction of the CPUC. The FERC has jurisdiction to set the rates, terms and conditions of service for PG&E's electricity transmission operations and wholesale electricity sales.

The California Energy Crisis and PG&E's Bankruptcy

As a result of the California energy crisis, PG&E filed a voluntary petition for relief under the provisions of Chapter 11 on April 6, 2001. PG&E retained control of its assets and was authorized to operate its business as a debtor-in-possession during its Chapter 11 bankruptcy proceeding. PG&E Corporation and the subsidiaries of PG&E, including PG&E Funding LLC, which issued rate reduction bonds, and PG&E Holdings LLC, which holds stock of PG&E, were not included in PG&E's Chapter 11 proceeding.

PG&E emerged from Chapter 11 when its plan of reorganization became effective on April 12, 2004. The plan of reorganization incorporated the terms of the Chapter 11 Settlement Agreement. Although PG&E's operations are no longer subject to the oversight of the bankruptcy court, the bankruptcy court retains jurisdiction to hear and determine disputes arising in connection with the interpretation, implementation or enforcement of (1) the Chapter 11 Settlement Agreement, (2) the plan of reorganization and (3) the bankruptcy court's December 22, 2003 order confirming the plan of reorganization. In addition, the bankruptcy court retains jurisdiction to resolve remaining disputed claims.

See Appendix A for a current list of PG&E's Corporate Officers and Board Members.

PROJECT DESCRIPTION / FINANCING STRUCTURE

On May 24, 2005, the I-Bank issued bonds (2005 Bonds) totaling $453,550,000 as auction rate securities (ARS) insured by Ambac Assurance Corporation (Ambac). The 2005 Bonds proceeds repaid loans that were used to pay-off prior bonds previously issued by the California Pollution Control Financing Authority (CPCFA Bonds) as a result of PG&E's bankruptcy filing in 2001. The CPCFA Bonds were used to finance costs of air and water pollution control as well as sewage and solid waste disposal facilities for two projects: PG&E's former Geysers Geothermal Power Plant comprised of geothermal electric generating facilities located in Lake and Sonoma Counties (currently owned by Calpine Corporation through Geysers Power Company, LLC) and Diablo Canyon Nuclear Power Plant.

Subsequent to the issuance of the 2005 Bonds, in early 2008 the ARS market became severely damaged due to credit risk problems related to the sub-prime mortgage market resulting in failed auctions and spikes in interest rates. During this time, interest rates of the 2005 Bonds reset as high as 10% substantially increasing borrowing costs for PG&E. In March and April 2008, PG&E elected to repurchase the 2005 Bonds in accordance with US Treasury guidelines to mitigate the high interest rates caused by the failure of the ARS market.

Additionally, Ambac's credit rating was downgraded from AAA to Aa3/AA by Moody's Investor's Service (Moody's) and Standard & Poor's (S&P), respectively, in June 2008 due to Ambac's reported financial losses also related to the continued sub-prime mortgage crisis.

PG&E has now requested the I-Bank to issue its refunding revenue bonds (2008 Bonds) in an amount not to exceed $453,550,000 to assist in refinancing the 2005 Bonds. The 2008 Bonds are expected to be sold and delivered to PG&E in exchange for the 2005 Bonds, thereby refinancing the 2005 Bonds. Concurrently with the exchange of the 2008 Bonds for the 2005 Bonds, the 2005 Bonds will be cancelled.

Once exchanged, it is expected that the 2008 Bonds will be resold on the secondary market as a combination of publicly-offered variable-rate demand bonds and fixed rate demand bonds. A portion of the 2008 Bonds to be resold are expected to be secured by direct-pay letters of credit while the remaining portion of the 2008 Bonds to be resold are expected to be unenhanced and carry PG&E's underlying rating. PG&E is currently rated A3/BBB+/A by Moody's, S&P and Fitch Ratings, Inc., respectively. All three rating agencies have recently upgraded PG&E's rating citing improved financial performance, a favorable regulatory environment and narrow strategic focus on regulated utility operations.

The 2008 Bonds shall constitute a special obligation of the I-Bank, payable solely from revenues or other sources provided for under one or more loan agreements between the I-Bank and PG&E. Neither the faith and credit nor the taxing power of the I-Bank, the State or any political corporation, subdivision or agency of the State will be pledged to the payment of the principal of, premium, if any, or interest on the 2008 Bonds, nor shall the I-Bank the State or any political corporation, subdivision or agency of the State be liable or obligated to pay the principal of, premium, if any, or interest on, the 2008 Bonds.

PUBLIC BENEFITS

Pursuant to a long-standing commitment by PG&E, ensured by the regulatory oversight of the CPUC, PG&E's electric and gas rates are set to cover PG&E's interest expenses. The vehicle for passing this benefit along to PG&E customers is the CPUC's annual cost of capital proceeding. In that proceeding, PG&E provides a listing of all its outstanding debt, as well as any projected changes, for the CPUC's review and approval. The interest expense that is approved by the CPUC is then incorporated into electric and gas rates charged to customers. PG&E estimates that the CPCFA Bonds and the 2005 Bonds have saved PG&E California customers as much as $7.7 million per year in interest expense.

If a tax-exempt refunding were not possible, PG&E probably would replenish the $453,550,000 withdrawn from its general treasury funds by arranging for the 2005 Bonds to be redeemed using proceeds of higher cost taxable debt issued with similar terms to maturity and with a similar mix of fixed-rate and variable rate debt.

To avoid continued higher borrowing costs on the 2005 Bonds due to the ARS structure and the presence of the Ambac insurance, PG&E anticipates that the exchange of 2008 Bonds for the 2005 Bonds will save an estimated $55 million for customers on a present value basis over the next 18 years.

EXHIBIT A

OTHER PROJECT DATA

PERMITS AND APPROVAL	
Required?	☒ **NO** ☐ **YES, Describe:**
TEFRA	
Date of TEFRA	Not applicable, the proposed exchange is covered under the TEFRA held for the 2005 Bonds.
Publications	
Oral/Written Comments	☒ **NO** ☐ **YES, Explain:**
LEGAL QUESTIONNAIRE	
Completed?	☐ **NO** ☒ **YES**
Issues?	☒ **NO** ☐ **YES, Explain:** PG&E has numerous lawsuits outstanding at any given time. As a publicly traded and regulated corporation, material information concerning the financial position and pending lawsuits and investigations are available to the public.
ELIGIBILITY REVIEW	
Project meets Public Interest Criteria (per G.C. §63046) ☒ **YES** ☐ **NO**	4. Project is in the State of California. 5. PG&E is capable of meeting the obligations incurred under relevant agreements. 6. Payments to be made by PG&E to the I-Bank under the proposed financing agreements are adequate to pay the current expenses of the I-Bank in connection with the financing and to make all the scheduled payments. 7. The proposed financing is appropriate for the Project.
Project meets Policies and Procedures established for the expeditious review of applications?	☐ **NO** ☒ **YES**
INDUCEMENT CERTIFICATE	
Completed?	☐ **NO** ☐ **YES** Certificate No.: ☒ **N/A** Date:

RECOMMENDATION

Staff recommends approval of Resolution 08-25, for an amount not to exceed $453,550,000 for Pacific Gas and Electric Company.

EXHIBIT A

APPENDIX A

Names and Titles of PG&E's Corporate Officers

Arndt, William (Bill), Vice President, T&D Business Operations; Interim: Vice President, Project Management and Program Office
Barcon, Barbara L,. Vice President, Finance and Chief Financial Officer
Basgal, Ophelia B., Vice President, Civic Partnership and Community Initiatives
Becker, James R., Site Vice President, Diablo Canyon Power Plant
Bell, Desmond Vice President, Shared Services and Chief Procurement Officer
Bottorff, Thomas E., Senior Vice President, Regulatory Relations
Burt, Helen A., Senior Vice President and Chief Customer Officer
Cairns, Stephen J., Vice President and Controller
Cheng, Linda Y.H., Vice President, Corp Governance & Corp Secretary
Cherry, Brian K., Vice President, Regulatory Relations
Conway, John T., Senior Vice President and Chief Nuclear Officer
Hapner, Dede, Vice President, FERC and ISO Relations
Harper III, William H., Vice President and Chief Diversity Officer
Hartman, Sanford L., Vice President and Managing Director, Law
Hayes, William D., Vice President, Maintenance and Construction
Howard, Robert T., Vice President, Gas Transmission and Distribution
Johns, Christopher P., Senior Vice President & Treasurer
Johnson, Mark S., Vice President, Electric Operations and Engineering
Keenan, John S. (Jack), Senior Vice President and Chief Operating Officer
Kiraly, Gregory K., Vice President, Maintenance & Construction
Kuga, Roy M., Vice President, Energy Supply
Lawicki, Patricia, Senior Vice President and Chief Information Officer
Livingston, Randal S., Vice President, Power Generation
Martinez, Placido J. (P.J.), Vice President, Transmission and Substations
McFadden, Nancy E., Senior Vice President, Public Affairs
Mistry, Dinyar B., Vice President, Regulation and Rates
Morrow, William T., President and Chief Executive Officer
Salas, Edward A., Senior Vice President, Engineering and Operations
Simon, John R., Senior Vice President, Human Resources
Wan, Fong, Vice President, Energy Procurement
Whitcomb, Bradley E., Vice President, Marketing and Customer Innovation
Williams, Geisha J., Senior Vice President, Energy Delivery

Pacific Gas and Electric Board

David R. Andrews
C. Lee Cox
Peter A. Darbee
Maryellen C. Herringer
Richard A. Meserve
Mary S. Metz
William (Bill) T. Morrow
Barbara L. Rambo
Barry Lawson Williams